

Asset Management Department

Market Perspectives

Setting the Stage for Monetary Easing

July 2024

Asset Management Department

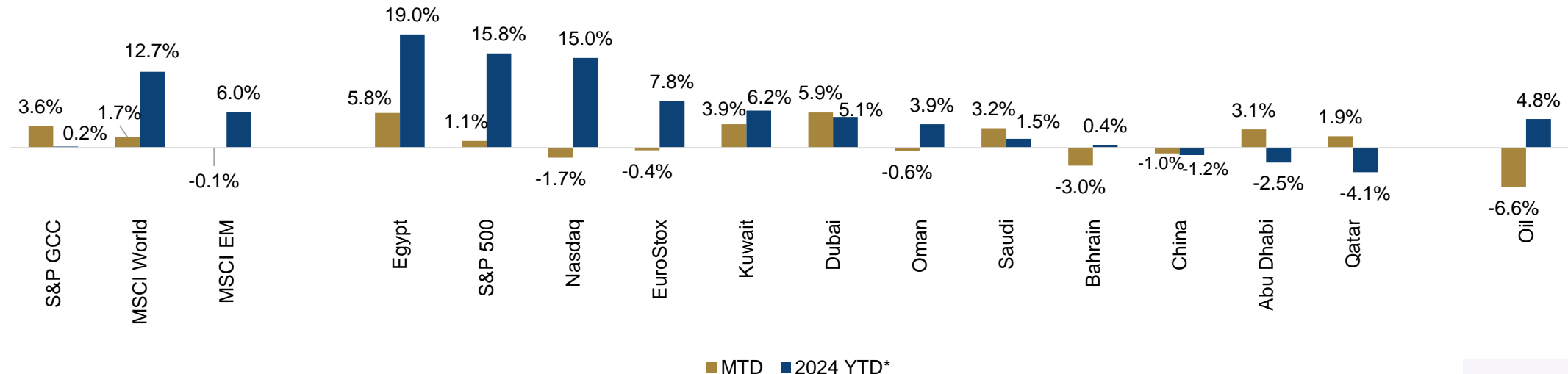
Section 1

Markets Performance

Equity Markets Performance

- The equity market performance was mixed during the month. The S&P 500 and MSCI World Index both remained almost flat, while the Nasdaq Composite down -1.6%. This downturn was driven by concerns over stretched valuations in a market led by mega-cap tech stocks coupled with skepticism surrounding CAPEX on AI and its foreseeable ROI.
- Investor uncertainty combined with potential rate cut in September led to a rotation out of tech-heavy indices into other sectors and smaller-cap stocks. As a result, while the Nasdaq declined, the Russell 2000 Index, which tracks small to mid-cap equities, surged by 11% during the month.
- Regionally, the S&P GCC index rose by 3.6% in July, reflecting overall positive sentiment across the region, driven by strong performances in key markets like Dubai up +5.9% and Saudi Arabia up +3.2%.
- The positive sentiment in the Gulf region, driven by sustained oil prices and economic reforms, reflects strong investor confidence. The region's \$2 trillion planned construction spending over the next five years, coupled with anticipated interest-rate cuts in 2H 2024, is set to boost equities. Lower rates are expected to be a key catalyst for Gulf markets, which are set to benefit index heavy weight Banks and Real estate.

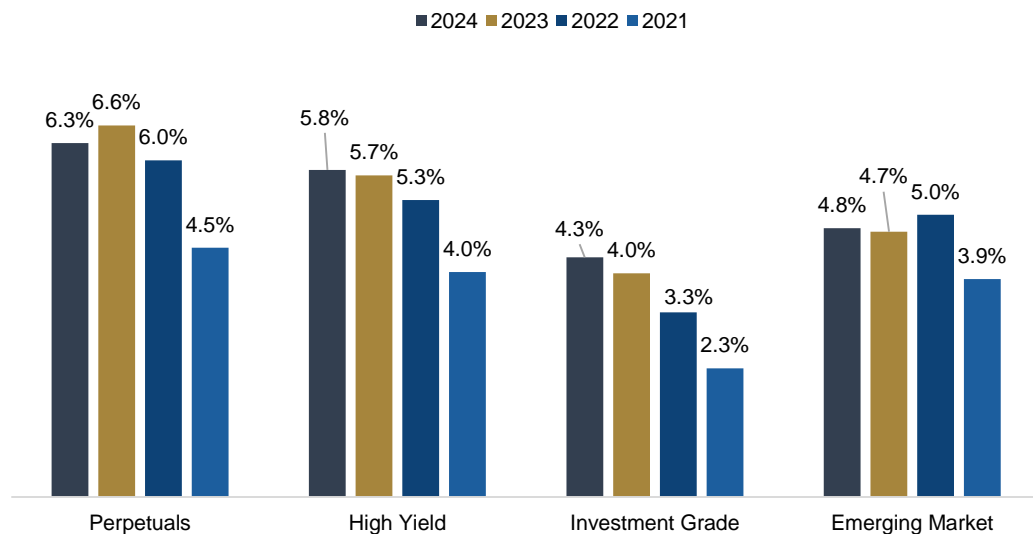
Global and Regional Equity Market Performance (ranked by YTD performance)



Fixed Income Markets Performance

- After a weaker than expected July job data report, the Fed is expected to cut rates by 25 basis points consecutively in September, November, and December to stimulate the economy, with a potential 50 basis point cut in September. This shift has led to a significant drop in 10-year Treasury yields by about 35 basis points to 3.82%, while the VIX spiked from 16 to 26, indicating increased market volatility.
- Investment-grade corporate bonds and quality MBS, particularly agency mortgage securities, remain attractive due to high coupons and reduced refinancing risk, supported by slow home sales and stable supply dynamics.
- The high-yield bond market benefits from higher yields and lower duration, with recent improvements in credit quality and low default rates. Despite economic uncertainties, high-yield bonds in defensive sectors, such as energy, offer attractive investment opportunities due to their resilience and potential for strong returns.
- GCC bond and sukuk issuances have exceeded expectations, driven by high oil prices and strong project pipelines. The region's bond markets are poised to benefit from potential US rate cuts and continued strong issuance, supported by stable currency pegs and robust economic conditions.

Fixed Income Yields

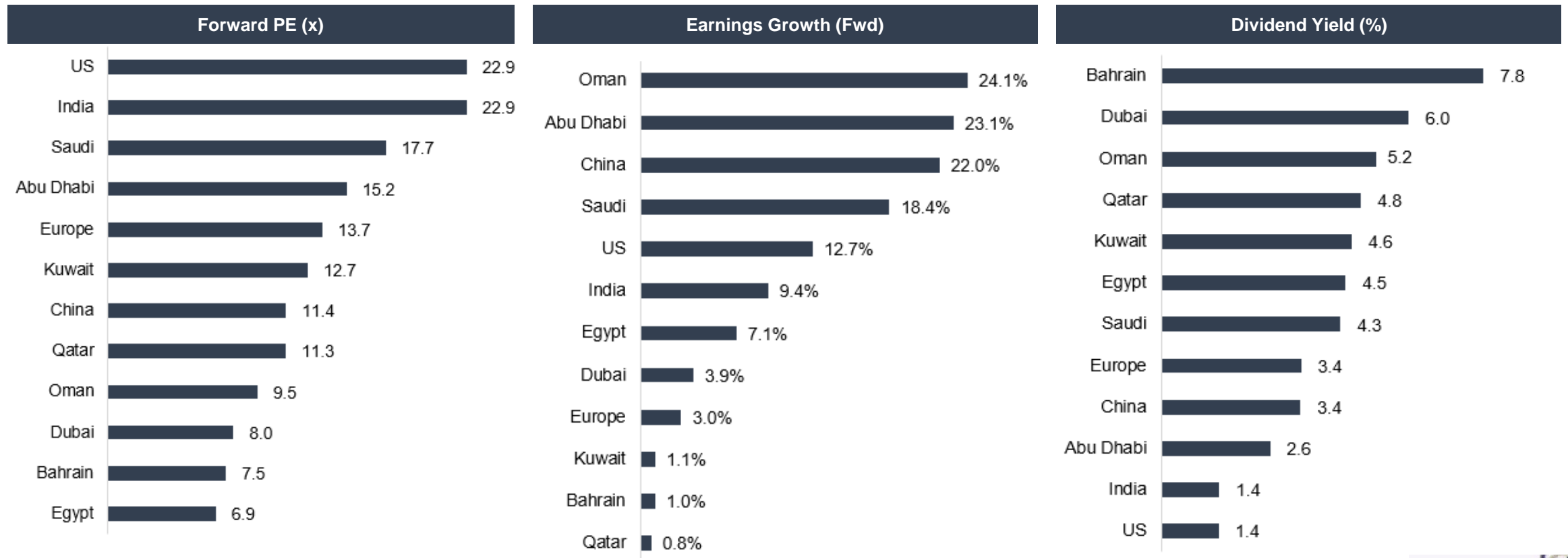


Bloomberg indices Performance

Indices	MTD	2024 YTD
Emerging Markets	2.2%	1.6%
Investment Grade	2.3%	-1.0%
Sukuk	0.9%	-0.4%
Corporate High Yield	2.2%	1.6%

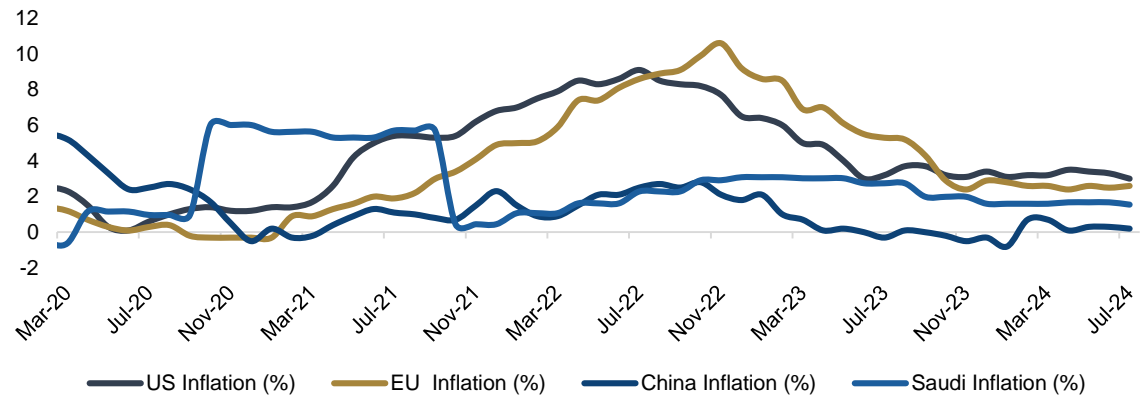
Relative Valuations

- U.S. valuations continue to exceed historical averages, primarily driven by strong performances from mega-cap tech companies. Despite this, valuations remain stretched, but are largely justified by robust earnings growth. The U.S. market is currently priced for a perfect scenario, with any earnings misses leading to significant market corrections.
- China's forward valuations remain near 10-year lows, indicating significant potential for growth. Recent signs of industrial recovery and economic diversification coupled with government stimulus packages are setting a positive outlook in the long-term.
- GCC markets are buoyed by structural growth driven by economic diversification and substantial government spending. Higher dividend yields, especially in the energy and financial sectors further enhance the relative appeal of GCC equities, supporting strong regional valuations.

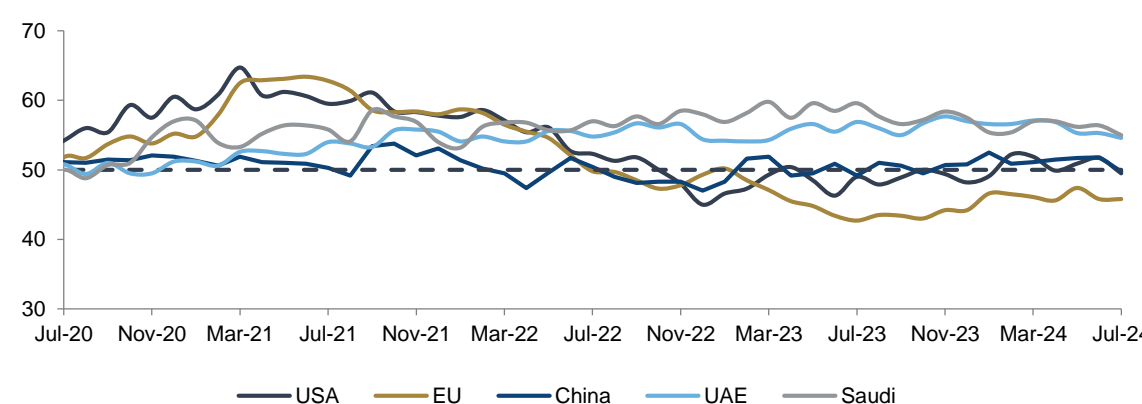


Economic Indicators

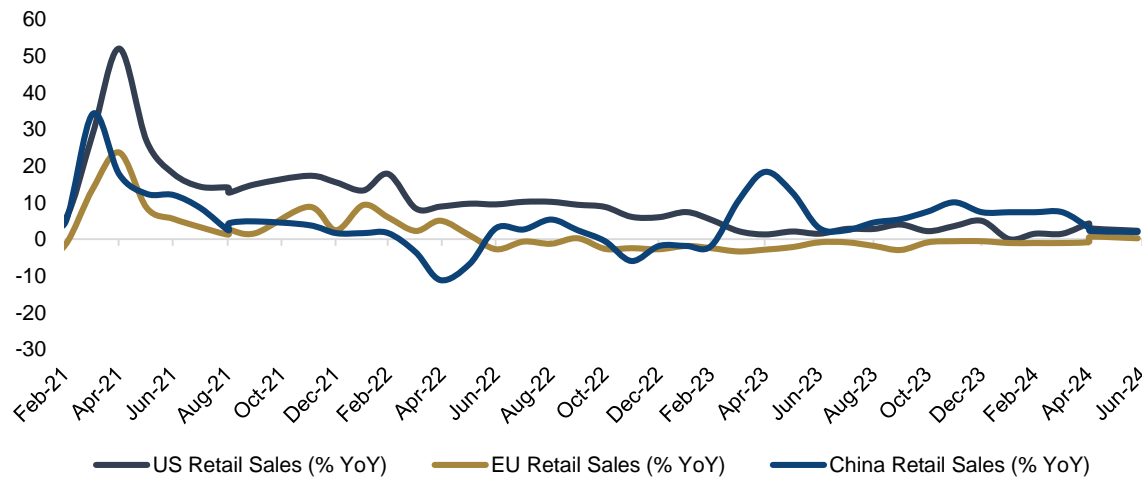
Headline Inflation (%)



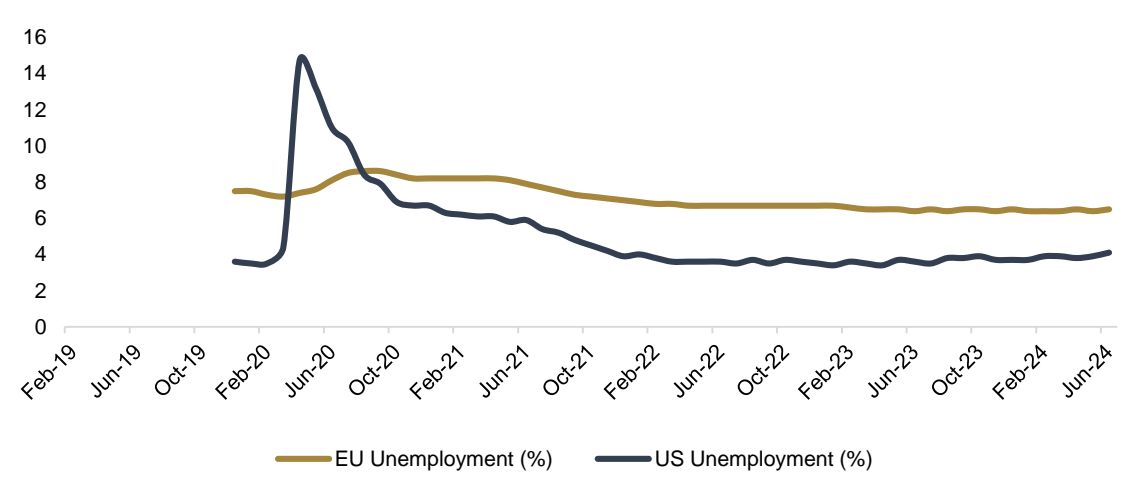
Manufacturing Purchasing Manager Index (PMI)



Retail Sales (%)



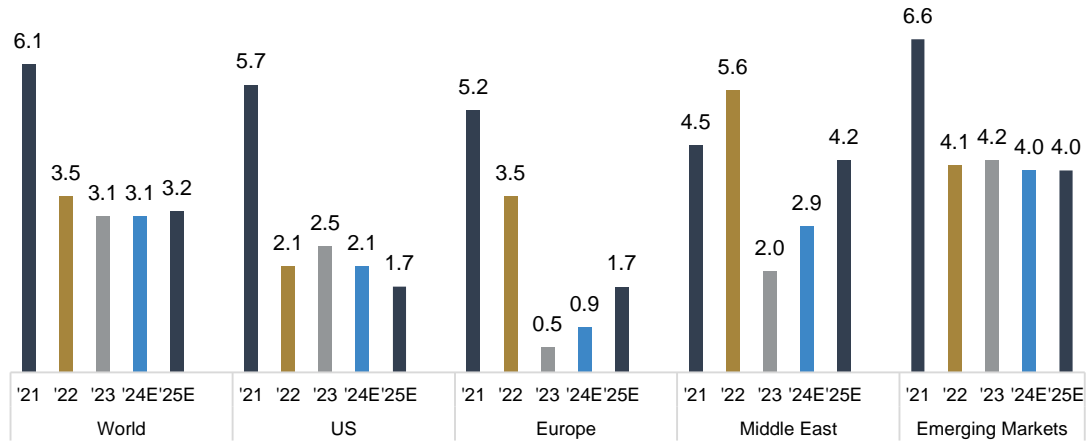
Unemployment Rate (%)



Macro Forecasts— IMF

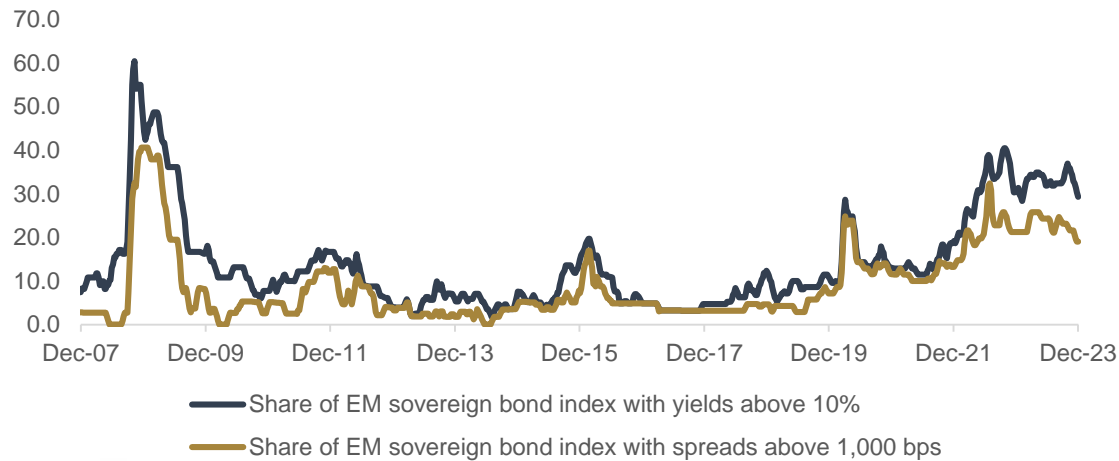
IMF Global Growth Forecasts (%)

IMF ups global growth for 2024 and 2025

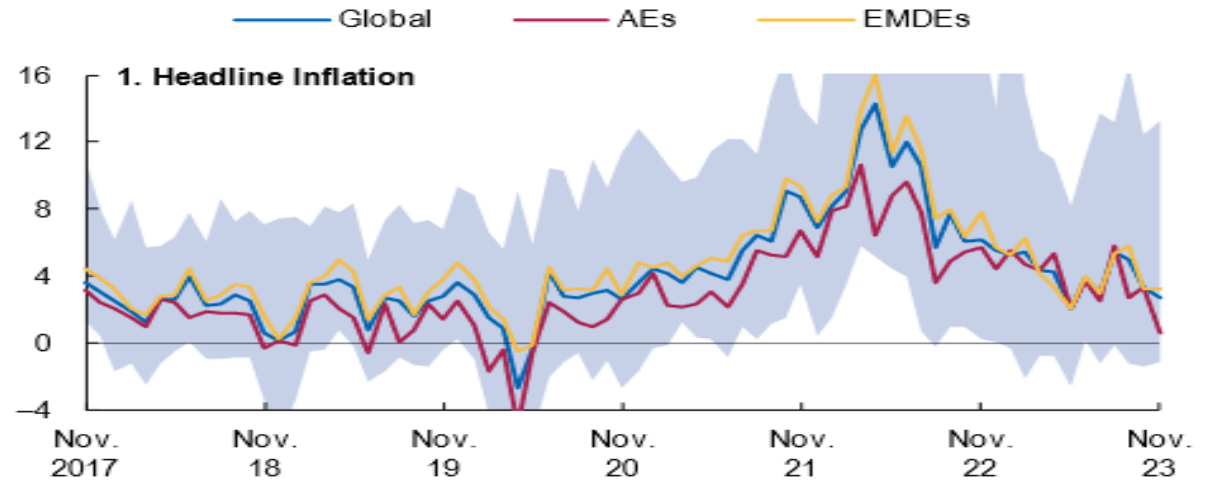


EM default spreads normalizing with yields still higher— EM is a theme for 2024

EM Fixed Income trade at attractive valuations

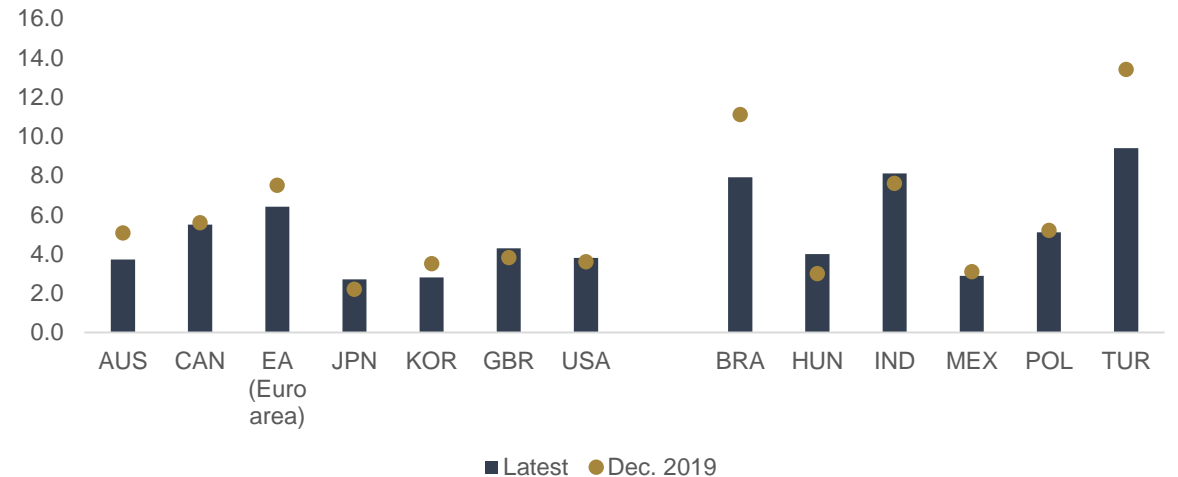


Global Inflation: Rise and Fall



Unemployment rate (%)

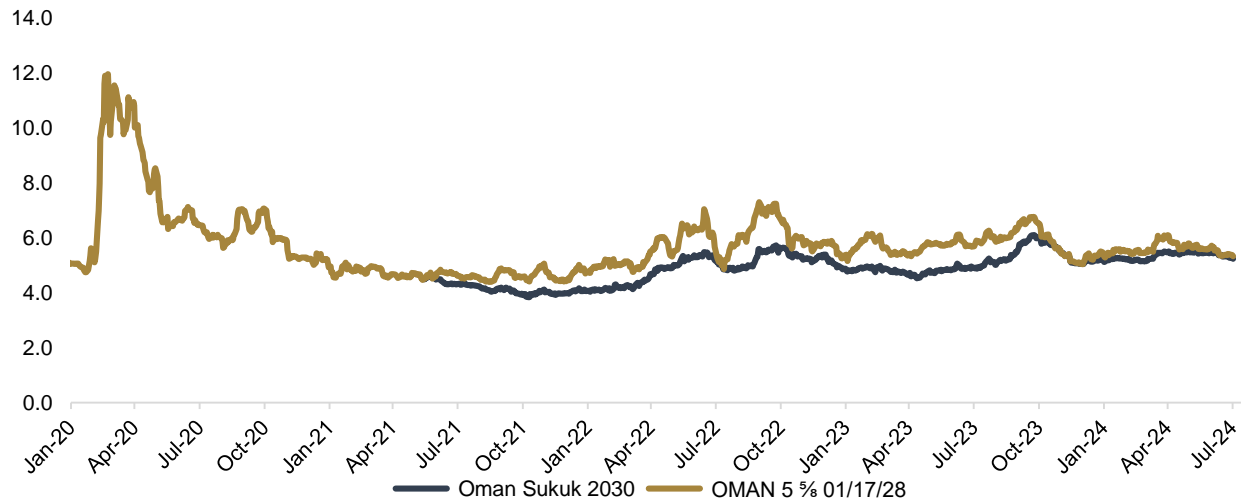
Labor market still tight but easing



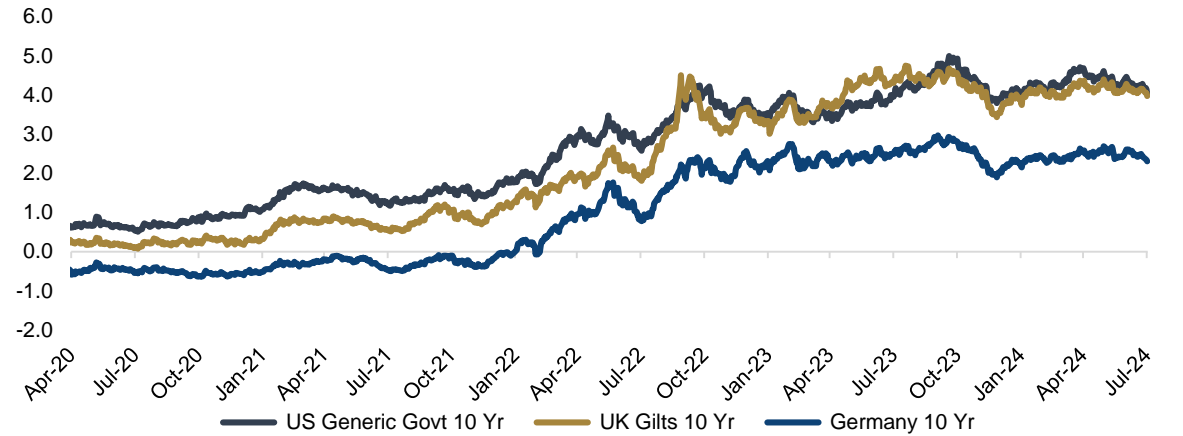
Fixed Income Monitor

Credit Default Swaps	Yields	MTD Change	YTD Change
Global High Yield To Worst	8.00	-0.26	-0.20
EM USD Aggregate YTW	6.90	-0.26	-0.14
ABUDHAB CDS USD SR 5Y D14	39.04	-4.66	-2.58
DUBAI CDS USD SR 5Y D14	70.87	0.00	7.64
BHRAIN CDS USD SR 5Y D14	194.58	0.00	-10.65
QATAR CDS USD SR 5Y D14	39.16	-4.18	-5.89
KSA CDS USD SR 5Y D14	57.18	1.48	4.53
OMAN CDS USD SR 5Y D14	103.52	0.00	-12.98

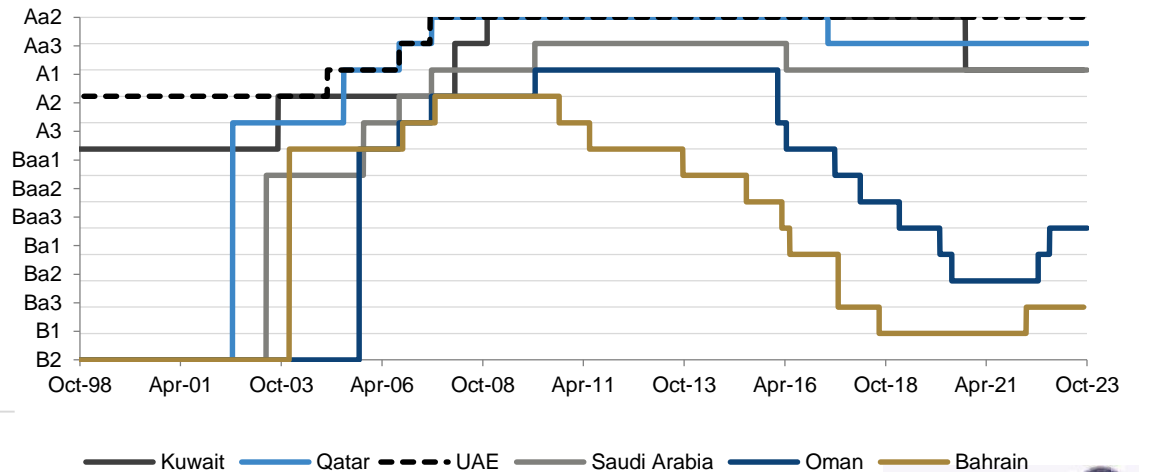
Oman Government Bond Yields



10 Year Yields



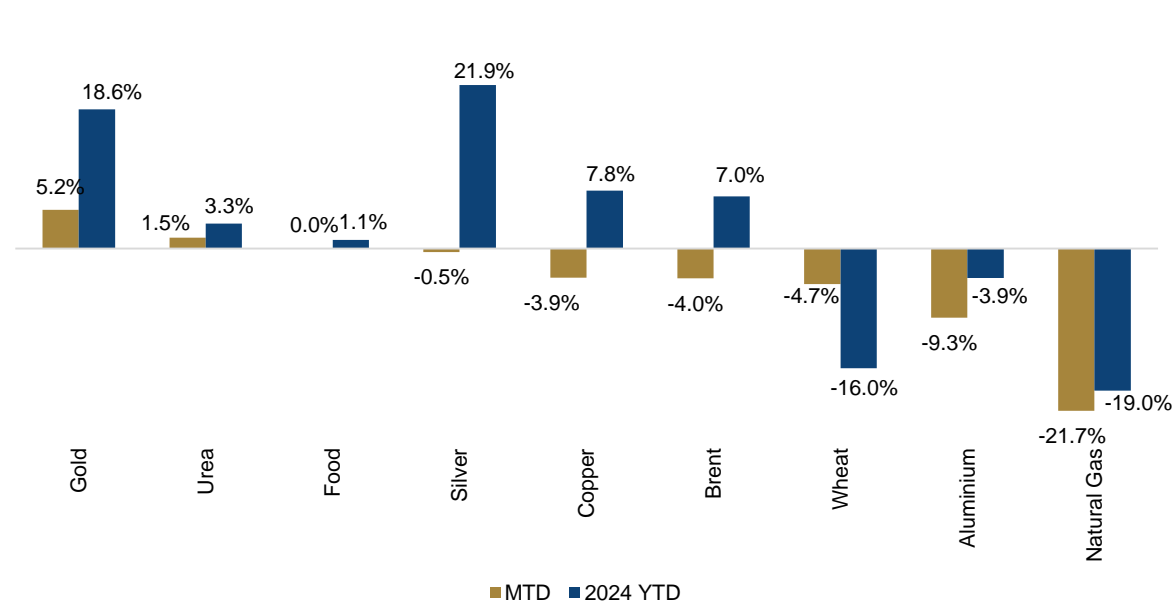
GCC Long-term issuer rating (foreign) by Moody's



Oil & Commodity Price Outlook

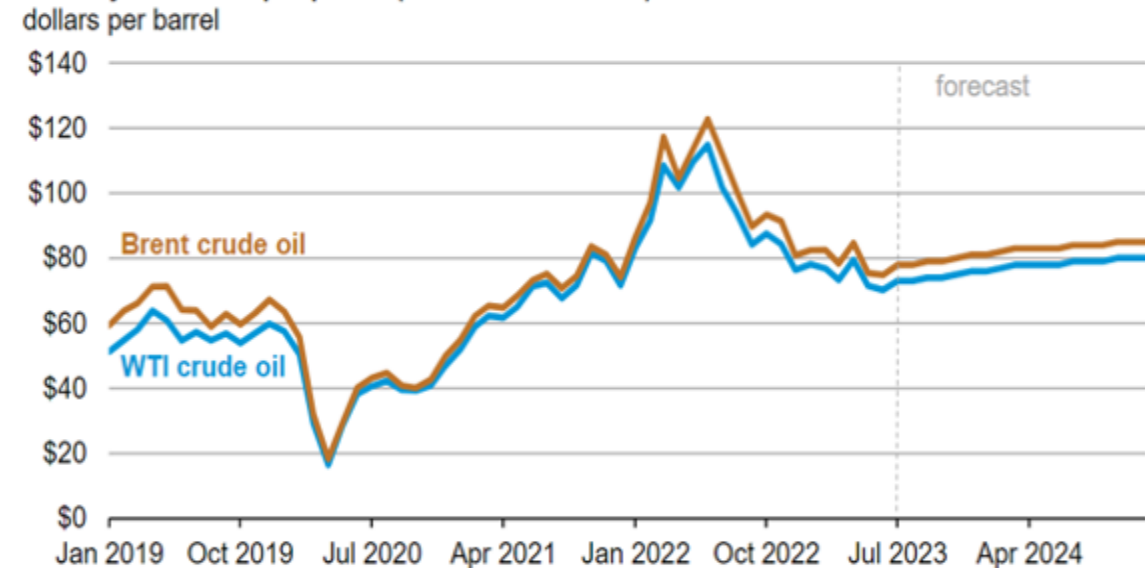
- Despite a decrease in Oil prices during July, Brent crude prices are supported reaching \$87 per barrel in the first half of 2024. This rise is attributed to strong global economic growth, OPEC+ production cuts, and heightened geopolitical risks, particularly in the MENA region, which are supporting Brent prices.
- Global oil demand is projected to grow by 2.2 mb/d in 2024, reaching an average of 104.5 mb/d, supported by a 2.9% forecasted increase in global economic growth.
- Non-OECD countries are set to account for the majority of oil demand growth, with a forecasted increase of 2.1 mb/d in 2024, while OECD demand is expected to grow by 0.2 mb/d. OPEC+ cuts are bolstering oil prices, and the geopolitical risk premium in the MENA region continues to influence market stability and pricing.
- For Copper, the latest COTR report reveals a significant reduction in investor bullish positions for copper, down by 5,760 lots to 65,467 lots, marking the lowest level since early February 2024. This decline reflects growing concerns about weakening demand in China, following three consecutive weeks of decreased positions.
- Gold prices have continued their upward trend, trading near all time highs of \$2,400/oz amid rising geopolitical tensions in the Middle East.. This is driven by market anticipation of potential Federal Reserve rate cuts in the upcoming meeting, which is bolstering demand for safe-haven assets.

Commodity Performance (ranked by MTD Performance)



EIA forecasts crude oil prices will increase through 2024 as demand rises above supply

Monthly crude oil spot prices (Jan 2019–Dec 2024)



Section 2

Investment Outlook

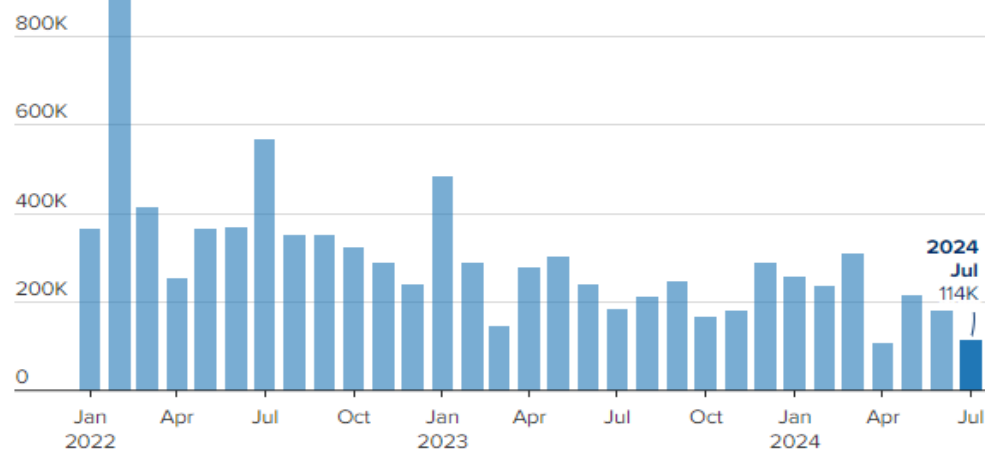
Key Themes

1 Fed Policy Outlook

- Weak July job data has led to expectations of a 25bps Fed rate cuts in September, November, and December, with a possible 50bps cut in September.
- However, recent data has shifted market sentiment:
 - ISM Manufacturing PMI dropped to 46.8 from 48.5
 - Non-Farm Payrolls fell to 114K from 179K
 - Unemployment rate rose to 4.3% from 4.1%
- The tone of the market has changed, with strategists suggesting that the Fed needs to cut rates not to normalize monetary policy, but rather to stimulate the economy.
- Despite concerns, the chances of a hard landing remain low, as the Fed has room to stimulate the economy with the Fed Funds rate at 5.25-5.55%.

Monthly job creation in the U.S.

January 2022 through July 2024

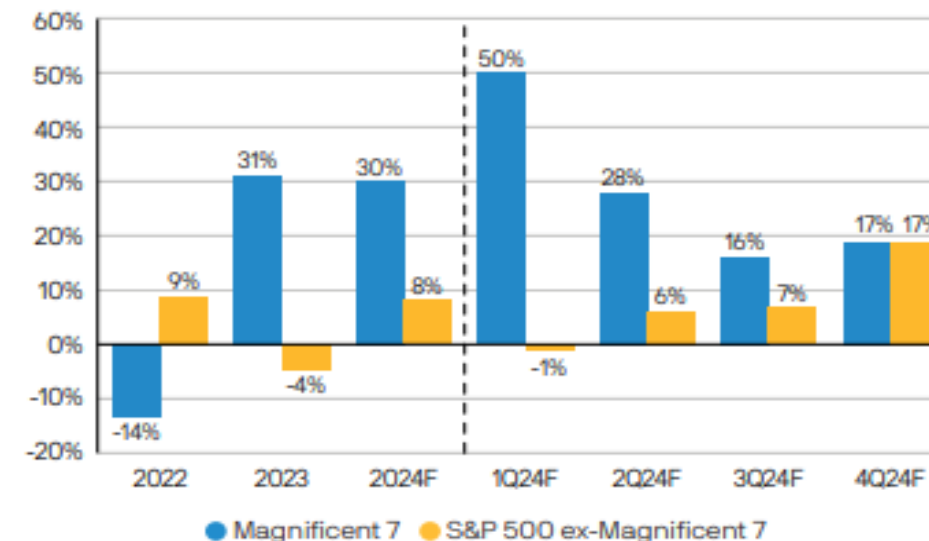


2 Signs of a Broadening of the Equity Rally

- The rally in the first half of the year was driven by the 'Mag 7', but there are signs of it broadening out, supported by strong corporate earnings and wide sector participation.
- Corporate America had a strong showing in Q1, with a 5% YoY EPS growth and significant earnings surprises across sectors. Every S&P 500 sector is expected to deliver both sequential and annual growth by Q4, a feat not seen since Q2 2021.
- Despite near-term vulnerabilities like economic uncertainties, stretched valuations and geopolitical tensions, equity valuations remain justified by higher earnings growth with further acceleration in 2025, driven by solid revenue growth and stable margins, ensuring long-term market performance

A broadening out in earnings growth is underway

Exhibit 7: Earnings growth



Key Themes

3 The Rotation Continues

- Anticipations of a Fed lowering borrowing costs in September have bolstered the small-cap segment, helping the Russell 2000 Index to narrow the gap with the Nasdaq 100 and the S&P 500.
- Small caps have a track record of generating strong returns following the dissipation of extreme mega-cap concentration and during US election years. This historical trend suggests a favorable outlook for small-cap stocks in the short-term.
- Small-cap and value shares are now outperforming the large-cap growth stocks that previously led the market, indicating a potential shift in market dynamics.
- The best strategy to access small caps involves a disciplined, fundamental approach. This ensures capturing outsized opportunities while avoiding unprofitable companies, capitalizing on the broader rally.

YTD U.S Indexes Performance



4 Outlook on GCC Banks

- Lending in the GCC is set to benefit in 2H from anticipated US rate cuts, oil prices at \$80+, and a \$2 trillion construction pipeline, provided geopolitical risks are contained.
- Easing monetary policy supports stable asset quality, but real estate oversupply poses recovery challenges, particularly for Qatari banks
- Lower interest rates may impact UAE banks' profitability in 2025 with rising provisions, while Saudi and Omani banks may maintain stable margins.
- The overall environment for Gulf financials remains positive, with growth driven by infrastructure investments and strong economic activity.

Key Drivers

Moderating Interest Rates	Oil at Least \$80	\$2 Trillion Construction Spending and Green Debt
BI View: Gradual Fed rate cuts should be supportive for Gulf banking profitability, particularly Saudi and Qatar lenders, as they're challenged by an inability to pass on higher rates without hurting asset quality and funding pressure that hampers margin.	BI View: Oil prices at least \$80 per barrel across the Gulf region are needed to support liquidity in the banking sector. Saudi Arabia is an exception, with the oil price likely needed to be \$100 a barrel to balance the budget and meet spending needs. Liquidity in the Saudi banking sector remains tight.	BI View: The Gulf region construction pipeline may reach \$2 trillion in the next five years, of which Saudi Arabia has the lion share of \$680 billion, followed by UAE at \$318 billion. This can be funded from local liquidity, suggesting there is an opportunity for debt issuance and green finance.
Companies: Saudi Fransi, Riyad Bank, Al Rajhi, Al Jazira, Qatar Commercial Bank and Al Rayan	Companies: Saudi Fransi, Riyad Bank, Al Rajhi, ANB, Doha Bank, Qatar Commercial Bank and Al Rayan	Companies: Saudi Fransi, Riyad Bank, Saudi British Bank, Alinma, QNB and Tawuniya

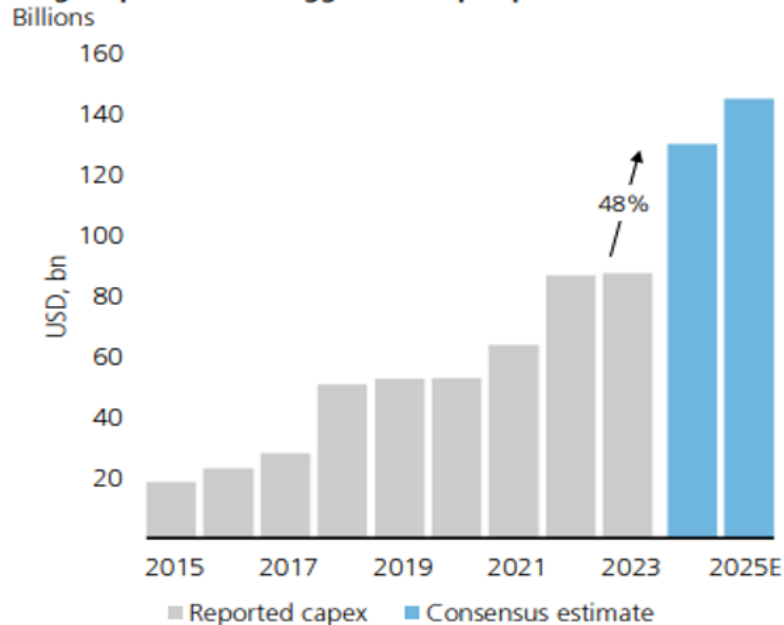
Key Themes

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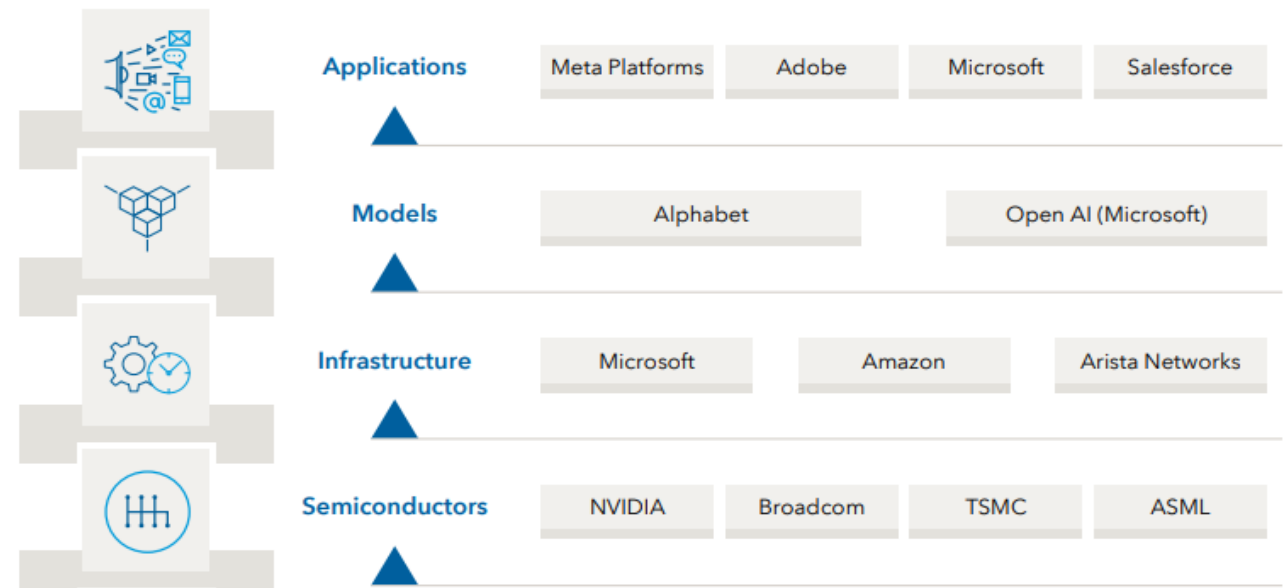
Opportunities in AI

- Generative AI is poised to revolutionize industries and societies, with leading tech giants and other companies expected to spend an estimated ~\$1 trillion on AI infrastructure and related capital expenditures in the coming years
- Success in AI investment hinges on comprehending the four layers of the AI stack — semiconductors, infrastructure, applications, and AI models. Key players like Alphabet, Meta, and Microsoft are heavily investing across these layers to secure their dominance.
- The AI trade can be divided into four distinct phases. Phase 1 focuses on Nvidia as the clear near-term AI beneficiary. Phase 2 highlights investment opportunities in AI infrastructure, encompassing semiconductor firms, cloud providers, data center REITs, hardware companies, security software stocks, and utilities. Phase 3 targets companies with business models that can incorporate AI to boost revenues, primarily software and IT services. Finally, Phase 4 includes companies poised for significant earnings growth from widespread AI adoption and productivity gains.
- Utilities can leverage AI for grid optimization, energy management, and grid security, making them attractive investment options in the AI landscape. AI can enhance demand forecasting, optimize energy consumption, and improve grid resilience against threats.

Mega caps announce aggressive capex plans for data centers



The AI stack consists of four essential layers



Section 3

Investment Strategy

Near-term Outlook

- Despite near-term vulnerabilities like stretched valuations and geopolitical uncertainty, equity valuations remain justified by higher earnings growth with further acceleration in 2025. This growth is driven by solid revenue increases and stable margins, ensuring long-term market performance. Our strategy prioritizes resilience by selecting high-quality stocks and bonds with low debt, robust margins, and strong cash flow visibility.
- Additionally, anticipations of the Fed lowering borrowing costs in September have bolstered the small-cap segment, helping the Russell 2000 Index to narrow the gap with the Nasdaq 100 and the S&P 500.
- Small caps, which have a track record of generating strong returns following the dissipation of extreme mega-cap concentration. This shift indicates a potential change in market dynamics. The best strategy to access small caps involves a disciplined, fundamental approach, ensuring the capture of outsized opportunities while avoiding unprofitable companies.
- We remain confident in the GCC market due to the positive sentiment, driven by sustained oil prices and ongoing economic reforms, reflects strong investor confidence. The region forecasted government heavy spending, coupled with anticipated interest-rate cuts in 2H 2024, is set to boost emerging-market equities

Near-term Outlook	Underweight	Neutral	Overweight	Comments
Equities				
US				Cautiously optimistic for US given recent rally and underlying strong breadth.
Europe				Neutral in Europe given easing inflationary pressures and attractive valuations.
Emerging Markets				Turned optimistic on EM markets as we see dollar strength wane.
MENA				Positive driven by support in oil prices but wary of geo-political risks.
Fixed Income				
US Treasuries				We have turned neutral in US treasuries as we see positive risk reward for non cash assets.
Global Investment Grade				We have turned positive on long duration investment grade bonds. CDS spreads widening to be key risk albeit risk is low.
Global High Yield				Turned neutral on Global High Yields given rising risk of credit defaults if growth slows
GCC Debt				Prefer Fixed Income securities linked to Sovereign or Financial Services sector

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